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Overview

While Ukraine's economic legislation is intended to provide a framework for business activities, it has lacked an integrated and publicly available analysis of its impacts on the development of a market economy in the country. Here we provide an independent evaluation of changes in the legal framework with regard to their impacts on market reform feasibility in Ukraine, and on the shaping of the investment climate and business environment. We suppose to publish such analysis annually scheduled for September, business and politic activities recommence after the summer break.

We evaluate policy intervention impacts of new economic legislation with regard to improvement or deterioration of the investment climate and business environment in Ukraine.

Policy intervention impacts of new economic legislation are evaluated with regard to improvement or deterioration of the investment climate and business environment in Ukraine. Policy is treated as a dynamic, focusing on changes passed since summer 1998 and outlining future developments.

Our analysis of new economic legislation involves the following steps:

- defining problems and issues that call for legislative action in shaping the investment climate and business environment in Ukraine;
- selecting legislative documents[1] designed to solve the above-defined problems;
- evaluating the impacts of the laws and decrees and their effectiveness in dealing with business issues;
- outlining prospects for future developments in legislation.

We chose the most important laws and presidential decrees passed in the period from April 1998 to September 1999 that had impacts in the areas of:

- regulation of businesses;
- taxation;

[1] The analysis focuses on laws of Ukraine adopted by the Parliament (Verkhovna Rada) and decrees of the President of Ukraine. In special cases, other types of documents are also considered.

- foreign trade;
- foreign direct investment;
- special economic zones;
- contract enforcement;
- privatisation and securities market development;
- regulations in the energy sector, agriculture, and banking.

The changing role of the government during Ukraine's transformation from a centrally planned to a market economy has resulted in a lack of consistency in developing a legal framework for business activities and investments.

The changing role of the government during Ukraine's transformation from a centrally planned to a market economy has resulted in a lack of consistency in developing a legal framework for business activities and investments. While the government's objective in a market economy is to provide a competitive environment for economic activities, actual decisions by the Ukrainian government, still burdened with the Soviet legacy, are biased towards tightening control over the economy. Consequently, legislative actions frequently negate each other, creating an uncertain business climate.

Although the Ukrainian Constitution declares the right to free economic activity, government approaches to regulation of businesses hardly adhere to this principle. Various government bodies interfere in the day-to-day activities of businesses, increasing their costs. The response of private businesses is to work in the shadow economy. The only way out is to develop a consistent regulatory framework, entailing greater transparency of regulation and redefining government functions.

A new approach to regulation is being implemented by ensuring compatibility of various government decisions with the goal of promoting competition. Consistency of the regulatory framework is achieved by the government doing cost-benefit analyses of interventions and evaluating their impact on incentives for businesses, as suggested by the draft Conception of the State Regulatory Policy[2]. Providing a competitive environment includes improving entry and exit regulations, simplifying registration and licensing procedures, and enforcing safety regulations. In addition, implementation of

[2] Developed by the State Committee for Entrepreneurship.

international accounting standards will facilitate entry of foreign businesses into Ukrainian markets.

Evolution towards better a taxation system in Ukraine primarily requires reduction of compliance costs and equalising the tax burden across different businesses. We consider that an important step forward in improving Ukraine's taxation was the passing of the presidential decree on a single tax for small and medium enterprises that significantly decreased compliance costs for businesses. Meanwhile, the tax policy aimed at providing incentives for businesses and investors is under risk, due to the lack of a balanced fiscal strategy. "Fire-fighting" measures to increase government revenues, including imposing additional taxes and levies, worsens the business environment by increasing the cost of doing business in Ukraine.

Foreign trade regulations are contradictory, consisting of declarations for trade liberalisation, on the one hand, and legislative decisions on augmenting protectionism, on the other. Ukraine's goal to join the World Trade Organisation requires liberalisation of foreign trade and abolishing export and import restrictions. Meanwhile, a series of protectionist legislative acts has been passed, including imposing export duties on scrap metals and sunflower seeds. Frequent and contradictory changes in foreign trade regulations contribute to uncertainty when making business decisions in Ukraine.

Lack of a balanced strategy aimed at improving the investment climate in Ukraine also impedes the development of a legal framework to encourage foreign investments. Foreign investors are given tenuous privileges in certain sectors instead of implementing an integrated policy to stimulate foreign investment. In particular, a series of documents has recently been passed on establishing special economic zones. Whereas the special economic zones are expected to attract foreign investments, there is a risk of growing government interference in business activities within these zones.

Long-awaited developments in contract enforcement include new bankruptcy procedures passed by amendments to the Law on Bankruptcy. The law stipulates a priority for claims on contracts with pledges. This procedure is expected to stimulate promotion of pledges as a mechanism for enforcing contracts. Enhancing contract enforcement mechanisms reduces the risks of business activities and promotes efficient resource allocation. Another improvement in contract en-

forcement is asset liability for tax debts, which replaces the *kartoteka* debt requisitioning system.

Institutional reinforcement of private ownership rights requires effective privatisation procedures. On the one hand, there is sufficient awareness of the necessity of cash privatisation that ensures selection of the most effective owners. On the other hand, political instability and vested interests impede successful implementation of cash privatisation. The delay in cash privatisation is hindering the development of a securities market, although much endeavour has gone into establishing the institution of a National Depository.

Finally, we picked up three specific sectors – agriculture, banking, and energy – that have endured most frequent government interference. Inconsistent government regulations increase the risks and costs of doing business in these sectors. Land reform is expected to reduce government interference in agriculture. Similarly, the National Bank's reliance on rules instead of discretion in banking regulation would increase the business attractiveness of this sector. Lastly, enhancing contract enforcement mechanisms in the energy sector is expected to improve payment compliance for energy supplies and to awaken market forces in this sector.

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Regulation of economic activity

Present methods and forms of state regulation of economic activity are based on principles inherited from the command-administrative system, as well as on management by total control. This approach was natural for the economy functioning under state ownership and planned management. Although during the past years a private sector has emerged in the economy, and a market with its own self-regulating mechanisms is being formed, the executive and its approach to the economy have remained unchanged. Government policy of direct interference in the economy is at odds with the market, which cannot develop under strict and unreasoned regulation.

The foundations for a regulatory reform were laid by the Presidential Decree "On eliminating limitations that restrain the development of entrepreneurial activity".

For the past year regulatory reform has been carried out in Ukraine, its foundation laid by the Presidential Decree dated February 3, 1998 "On eliminating limitations that restrain entrepreneurial development". This decree was the first to recognize the necessity of "taking measures to remove limitations that restrain business development, and reduce excessive state regulation of business (deregulation)". According to the decree, regulatory reform has two components: (1) a review of regulatory acts currently in force (to be conducted by the State Committee for Entrepreneurship and the Interagency Council for Business Deregulation); and (2) elimination of draft regulatory acts that hamper business development via establishing a reconciliation procedure with the SCE and the Licensing Chamber of Ukraine.

The Presidential Decree "On certain measures to deregulate entrepreneurial activity" settled the inspections issue.

The second important step of regulatory reform was the Presidential Decree dated July 23, 1998 "On certain measures to deregulate entrepreneurial activity", which settled the inspections issue. The document determines: (a) a list of state authorities that are empowered to conduct inspections of financial and economic activity on behalf of the government; (b) the types of inspections; (c) the procedure and reasons for conducting inspections; and (d) the number of inspections. But practical implementation of this decree has indicated that many of its clauses were not elaborated well, which allows controlling authorities to ignore them. As a result, the problem of excessive inspections has still not been resolved.

Law of Ukraine "On the sources of government financing" changes control authorities' incentives, prohibiting them from creating off-budget and charity funds.

In order to cope with the problem, a new approach to controlling entrepreneurial activity is needed (from total control over each entity to control over general indicators), and controlling authorities' incentives need to be changed. An important step towards this is the Law of Ukraine "On the sources of government financing" dated June 30, 1999. According to it, "state authorities are prohibited from creating off-budget funds, possessing special off-budget accounts, or using funds obtained from accomplishing state functions (these include issuing permits (licenses) and certificates, conducting registrations, and other activities on a paid basis) in any other way except their transfer to the State Budget". The law is supposed to remove the incentives to "over-inspecting" and creation of non-transparent regulations, which provoke violations on the part of entrepreneurs, leading to fines (30% of fines could be transferred to control authorities' off-budget funds). In addition, incentives to increase the number of license-requiring activities will diminish.

The upcoming Conception on State Regulatory Policy is the first step to systemic regulatory reform. The concept document envisages obligatory justification of the expediency and efficiency of government interference, as well as a continuous dialogue between state authorities and economic entities.

In general, regulatory reform showed that the measures undertaken at present are not sufficient to generate qualitative changes in business conditions. There is a need for a systemic change in regulatory policy. The first step is prepare of a concept document on state regulatory policy that envisages obligatory justification of the expediency and efficiency of government interference into a particular sphere (analysis of alternative means and justification of expenditures faced by entrepreneurs and the government resulting from the implementation of new regulations). Dialogue between state authorities and business must be introduced as well. As a result of such policy, government-business relations will become more transparent. Business will be able to protect its interests at the stage when new regulations are being worked out, which will improve the quality of government decisions.

Some steps have already been made. A common system of planning, co-ordination, and control over rule-making by executive authorities was established pursuant to the Presidential Decree "On measures to improve rule-making", dated February 9, 1999. This will make such activities more transparent and predictable.

There is also an immediate need for determining the role of non-governmental organizations, mechanisms for public debate of draft normative-legislative acts, as well as ensuring unrestricted access to information on rule-making activity.

These problems can potentially be solved by the laws "On laws and legislative activity in Ukraine" and "On normative-legal acts", which have already passed legislation in the first reading.

Entering and exiting the market

Entry/exit procedures depend on government policy on entrepreneurial activity and primarily on the extent of its market orientation. Entry to the market is a sequence of steps starting from creating a business entity and ending with obtaining necessary permits and licenses. Exiting the market entails liquidation of the business entity[3].

The registration procedure for businesses is determined, however the liquidation procedure is still not defined.

While a registration procedure for business entities has been determined, the liquidation procedure is still not defined (only some steps to be executed during liquidation are indicated, but many other issues are not covered in the procedure, thus they are solved non-systemically). Lack of motivation for proper liquidation of enterprises on behalf of their founders, and ambiguity of many issues in the liquidation procedure, have led to an accumulation of moribund enterprises. The new edition of the Law "On bankruptcy" (see **CONTRACT ENFORCEMENT**) prompts the need for a strict liquidation procedure.

The registration procedure for businesses is defined by the Law of Ukraine "On entrepreneurship" and Cabinet of Ministers Resolution "On the procedure for state registration of business entities".

Businesses register according to the procedure defined by the Law of Ukraine "On entrepreneurship" and Cabinet of Ministers Resolution "On the procedure for state registration of business entities" dated May 25, 1998. According to these documents, the state registration agency forms a business entity's registration case after data in the record card and

[3] While entering and, especially, exiting the market two main issues are "ownership" and "responsibility" (Law of Ukraine "On ownership" adopted on March 7, 1991, last changed on February 28, 1995). Obviously, owners and administrations of businesses carry out different functions and have different responsibility. But lately, due to ambiguity concerning the concept of "employer" in Ukrainian legislation, owners are in fact being saddled with administrative responsibility (especially by the Law of Ukraine "On foundations of legislation of Ukraine on obligatory state social insurance", dated January 14, 1998). The responsibility is confirmed by the draft law "On employers' organizations". This creates unequal conditions for owners of private enterprises, shareholders (of which there may be thousands), and, moreover, state-owned enterprises.

completeness of the document package are verified. The date of document receipt is fixed in the case registry and the applicant is informed about this in written form. If all the documents listed in the regulations are available, the state registration agency should put the data from the record card onto the List of Business Entities within five working days of their receipt. A state registration certificate with indicated corporate/individual person's identification code is issued.

The minimum amount for the statutory fund of limited liability companies was reduced from 625 to 100 minimum monthly wages by the Law of Ukraine "On making changes to some laws of Ukraine concerning the activities of economic entities".

One of the obligatory norms in creating a limited liability company is the statutory fund minimum amount, which is regulated by the Law of Ukraine "On economic entities" dated September 19, 1991. Until May 1999 this Law set the statutory fund minimum amount for limited liability companies at a level of 625 minimum [monthly] wages on a company's registration date (in May 1999 it was about $13 thousand). This led to a sharp decrease in the number of new entities registered as limited liability companies, although especially for small business this form is the most flexible and attractive. The minimum statutory fund amount for limited liability companies was lowered from 625 to 100 minimum [monthly] wages (based on the minimum [monthly] wage on the founding date) by the Law of Ukraine "On making changes to some laws of Ukraine concerning the activities of economic entities" dated May 5, 1999.

In order to achieve qualitative improvement in entry/exiting conditions a specific state policy should exist whereby the rate of new entities' foundation can serve as a measure of its effectiveness[4]. Policy results should include:

- further improvement in business foundation and registration procedures, especially a discontinuation of regulating the statutory fund minimum amount for limited liability companies;
- development of transparent procedures for business liquidation; announcements about liquidation com-

[4] World experience indicates that in developed countries the number of business entities accounts for 7–10% of the country's population. Thus, 5 million businesses can potentially exist in Ukraine. Currently there are about 800 thousand registered enterprises, 140 thousand of which are functioning (those who report to controlling bodies), and nearly 800 thousand entrepreneurs registered as individual persons.

mittees starting their work should be concentrated in a single place, for instance on a special Internet page.

Permit system

Ukraine lacks an integrated permit system, which has led to uncontrolled growth in the number of activities requiring permits or licenses.

Currently Ukraine lacks an integrated permit system, which leads to uncontrolled growth in the number of activities requiring permits or licenses.

State policy on the licensing of economic activities was determined in 1996 by the Cabinet of Ministers Resolution "On the development conception for a state system of licensing economic activities according to their types". Although according to the conception "only those economic activities that directly influence human health, environment, and national security are subject to regulation", the list of activities requiring licensing is constantly expanding.

Three new types of licenses were implemented during the last year alone–antidumping, compensatory, and special. They were aimed at protection from dumping and subsidised imports (laws of Ukraine dated December 22, 1998 "On the protection of national producers from dumping imports", "On the protection of national producers from subsidized imports", and "On special measures regarding imports into Ukraine"). The list of activities requiring licensing was extended to include:

- topographic, geodesic, and cartographic works (the Law "On topographic, geodesic, and cartographic activities", dated December 23, 1998);
- hydrometeorological activities (the Law "On hydrometeorological activities", dated February 18, 1999);
- trade in petrochemicals (Presidential Decree "On the state regulation of exports, imports, wholesale, and retail trade in petrochemicals", dated June 11, 1999);
- wholesale trade in sugar (the Law "On the state regulation of sugar production and sales", dated June 17, 1999);
- development, production, and sales of special technical devices for obtaining information off communication channels, and other devices for covert obtaining of information (the Law "On amending Article 4 of the Law of Ukraine 'On entrepreneurial activities'", dated January 12, 1999);

- eight types of activities in the transport and power sectors (Presidential Decree "On the implementation of licensing the activities of economic entities in the sphere of natural monopolies", dated November 17, 1998).

However, the situation with permits, certificates, and patents turns out to be much worse. In order to obtain a single license one typically needs a number of permits and consents. These forms of limiting economic activities are not regulated yet, and there is no exact information on their number, either. A step towards resolving this problem is the Presidential Decree "On introducing a permit system in the sphere of entrepreneurial activities" dated May 20,1999. It clearly stipulates that "licenses are the only permit document that give the right to engage in a particular economic activity, which is subject to limitations in accordance with legislation".

Regulation of reporting and accounting

On the one hand, issues of accounting, account and statistic reporting are strictly regulated by countless instructions, but on the other hand these instructions are subject to overly frequent changes, mainly due to changes in tax legislation. Another big problem is created for investors by the inconsistency of Ukrainian accounting norms with international standards; as a result a dual accounting regime is needed.

The Law "On accounting and financial reporting in Ukraine", dated July 16, 1999 will make accounting and reporting simpler and more modern.

In order to cope with these problems an important step has been taken. The Law "On accounting and financial reporting in Ukraine" was adopted on July 16, 1999. The law introduces new regulations, namely:

- defines the precise composition of financial reporting;
- introduces the concept of public reporting;
- for the first time recognizes the possibility of accounting being conducted at an enterprise by an outside specialized firm or entrepreneur-accountant;
- recognizes the legitimacy of primary accounting documents and registers created by machine (e.g., computers).

All these measures will make accounting and reporting significantly more simple and modern. Still, the main regulatory functions concerning accounting procedures and composition of reporting will be set by national standards, to be elaborated and approved by the Ministry of Finance based on international accounting standards. In order to guarantee that the standards will be adequate for economic activities and will not become worse, an advisory board (Methodological Council) will be set up according to the law. The board will consist of specialists and representatives of accountants and auditors' public associations.

Eight national accounting standards, which correspond to international standards, have already been adopted (overall there are about 30 international standards). The first five standards deal with financial reporting: "General requirements to financial reporting", "Balance", "Report on financial results", "Report on cash flows", "Report on capital". The sixth standard is procedural: "Mistakes correction and changes in financial reports". The 19th standard on "Enterprise mergers" has been adopted; it defines the procedure for representing other enterprise purchases and information on mergers in accounting and reporting. The 20th standard on "Consolidated financial reporting" has been adopted too; it regulates the required information on enterprise groups, i.e., associated (holding) companies and their affiliates.

Product safety and quality

To date the government has still not developed a holistic view of the state's role in product safety and quality regulation. The government still tries to regulate quality, though it is an entirely market-driven factor in competition for the consumer, by establishing numerous controlling bodies.

Currently the government lacks a holistic view of the state's role in product safety and quality regulation. None of the existing normative documents[5] defines the following: what is regulated concerning product safety and quality, how it is regulated, and who regulates the issue. The government still tries to regulate quality, while it is an entirely market-driven factor in competition for the consumer. The result of this is not an increase in quality, but increased government interference in competition, and artificial limitation of entrepreneurial activities.

The government's attempts to fulfil unnatural functions has led to the appearance of more than 15 state bodies that perform state control over product safety and quality. Very often

[5] State standards are not normative documents.

their functions duplicate each other and their responsibility is only declarative.

During the last year the problem became worse due to setting up a National Agency for Control over Quality and Safety of Food Products, Pharmaceuticals and Medical Products (Presidential Decree dated February 1, 1999). The Agency is to ensure state control over the quality and safety of certain types of food products. The situation is also aggravated by strengthening the authority of the Committee of Ukraine on Monopoly Production and Sales of Alcoholic and Tobacco Goods (Presidential Decree dated August 2, 1999).

The certification procedure in its current form increases the prices of goods, burdening them with non-production expenditures. Certificates of most developed industrial countries are not recognized by Ukraine.

The Committee of Ukraine on Standardization, Metrology, and Certification elaborated a conception of reforming the national standardization, certification, and accreditation systems that actually preserves the existing certification system. If the target is to increase business activity, then the conception needs fundamental changes. State regulation must be limited to issues of safety only. Accents need to be shifted to voluntary quality declaration. In this case an economic entity can be brought to responsibility if the real quality does not correspond to the declared one.

The Cabinet of Ministers, in its turn, has submitted to the Verkhovna Rada a draft law "On suppliers' responsibility for production and sale of low-quality and unsafe products". The idea of the draft law lies in shifting the controls over quality onto economic entities. But due to many unclearly-defined terms and procedures (for instance, the appeal procedure) implementing the law can lead to uncontrolled changes of civil and financial responsibility with respect to suppliers.

Taxation policy

The tax system in Ukraine is insufficiently oriented at stimulation of business and investment activities because of (1) high compliance costs faced by taxpayers, (2) unequal distribution of the tax burden, and (3) introduction of unjustified taxes in order to increase budget revenues. During the last year tax legislation underwent some positive changes, particularly concerning simplified taxation of small and medium businesses, and regulation of relations between taxpayers and the budget. The tax burden and compliance costs[6] have also partially decreased, resulting from cancellation of the Chornobyl Fund and 10% amortisation deductions to the state budget. However, rapid growth in the number of granted tax privileges, and constant debt restructuring and write-offs, have aggravated the inequality in tax burden distribution among economic entities. Moreover, resulting from the lack of a deliberate fiscal strategy, the government resorts to the introduction of additional taxes and levies for the purpose of quick budget revenues.

Compliance costs

Complicated procedures for calculating and accounting taxes are the main factor causing high compliance costs. Small and medium businesses are especially sensitive to this factor. Another factor is the instability of tax legislation

The main factor causing high compliance costs is the complicated procedure for calculating and accounting taxes. Small and medium business entities are especially sensitive to this factor. Another factor is the instability of tax legislation, which creates uncertainty in decision making on the part of economic entities. The uncertainty is increasing because the state is not meeting its commitments to taxpayers (particularly concerning VAT reimbursement).

The Presidential Decree "On some changes in taxation", dated August 7, 1998 was a step towards decreasing taxpayers' compliance costs. According to the decree, deductions to the Chornobyl Fund were cancelled starting from January 1, 1999. The cancellation of Chornobyl Fund payments had a greater effect on accounting procedures simplification than on diminishing the tax burden[7]. In accordance with ICPS's

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[6] Economic entities' compliance costs lie in the time and energy spent on calculating and accounting taxes.

[7] The levy was 10% and was calculated based on the wage fund. The sums paid were regarded as gross expenditures in calculating income tax. The cancellation of this levy diminished the wage fund

business activity survey[8], in the first quarter of 1999 the number of enterprise managers who indicated the wage fund accruals to be the most unfavourable tax decreased to 50.2% from 54% in the fourth quarter of 1998. At the same time, the share of respondents, who consider wage accruals to be the most complicated concerning their accounting procedures decreased from 44.7% in Q4'98 to 32.1% in Q1'99.

The Presidential Decree "On some changes in taxation" established the possibility for offsetting on VAT and advance VAT payment debts against the budget reimbursement of this tax. Moreover, the sum of the budget reimbursement may be accounted as payment of other taxes. This procedure allows economic entities to plan their cash flows more optimally and removes the uncertainty which emerged as a result of the state not meeting its commitments concerning VAT reimbursement.

The Presidential Decree "On the simplified taxation, accounting, and reporting system for small business entities" was the most important change in tax legislation for small and medium businesses. The first edition of the decree was adopted on July 3, 1998, though it did not lead to the desired outcome because the simplified system applied to a limited number of business entities. According to the last version of the decree, dated June 28, 1999, the simplified taxation will be extended to a much larger number of business entities, specifically, to individual entrepreneurs with sales incomes of less than half a million hryvnias per year (250,000 hryvnias in the previous edition), and legal entities with sales proceeds of not more than 1 million hryvnias per year (250,000 hryvnias in the previous edition). A fixed tax was introduced for individuals in amounts varying from 20 to 200 hryvnias per month. For legal entities the integrated tax rate makes up 6% of sales proceeds in case VAT is paid, and 10% in case VAT is included in the integrated tax.

The decree significantly simplifies the procedure for calculating and accounting taxes for small and medium business. The integrated taxpayers are exempt from accounting those

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accruals while enlarging the base for profit taxation. The decree also envisaged a decrease in the obligatory social security levy from 5.5% to 4.5% but this norm was repealed by the law of Ukraine dated September 30, 1998.

[8] Data of the Business Opinion Survey, an ongoing activity of the International Centre for Policy Studies.

taxes that were included in the integrated tax, specifically, profit tax, personal income tax, and wage fund accruals. Individual entrepreneurs are not obliged to use electronic cash registers. The flexibility of the proposed simplified taxation system (businesses have the possibility to choose the method of taxpaying) will promote its efficiency. The simplified accounting and reporting systems for small and medium enterprises will promote their increase in number, thus improving the overall competitive environment in the country.

Another document is the Law "On the fixed agricultural tax" dated December 17, 1998, which simplifies accounting and reporting systems for agricultural enterprises. It replaces 11 taxes with an integrated fixed tax charged according to farmed area. The fixed tax facilitated business activities in agriculture, though the positive effect on the level of competition will be minimal because the sector is over-regulated[9]. Thus the simplification of the taxation system in agriculture will not improve its effectiveness.

Instability of tax legislation is a negative factor that leads to an increase in taxpayer expenditures and decline of business activity. During the past year excise rates have been the most unstable element of tax legislation. The instability emerged owing to the lack of a single norm-making authority that would have an exclusive right to set excise rates[10]. Consequently, excise rates for some goods are regulated by several acts simultaneously. For instance, there are two documents currently in force that determine different excise rates for gasoline: the Law "On excise rates and import duties for some goods (products)"[11] and the Presidential Decree "On excise rates for oil products"[12].

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[9] Creation of agricultural enterprises is limited by the absence of a land market, the moratorium on agricultural enterprise bankruptcy, and e the state system for supplying inputs to collective agricultural enterprises.

[10] Excise rates have been changed by laws and presidential decrees. Moreover, during the period from June 18 till October 14, 1998 the Cabinet of Ministers was also granted the right to set excise rates.

[11] The law was adopted on July 11, 1996, with the most recent changes in excise rates for gasoline made on May 5, 1999.

[12] The decree was adopted on June 24, 1998, and changes were made on June 22, 1999.

The Law "On the procedure for setting tax and levy rates (compulsory payments), and other elements of tax bases, and also tax privileges" dated October 14, 1998 was aimed at resolving contradictions in the tax legislation. The Verkhovna Rada of Ukraine was determined as the only authority to make changes in tax legislation. By a resolution of the Verkhovna Rada dated December 24, 1998 the President was recommended to abolish his normative acts on taxation. Nevertheless, the law dated October 14, 1998 and the resolution dated December 24, 1998 are not being implemented in reality.

Inequality in tax burden distribution

Loose government policy on privileged taxation leads to unequal distribution of the tax burden among economic entities.

Loose government policy on privileged taxation leads to unequal distribution of the tax burden among economic entities. Besides the privileges defined by basic laws, some privileges remain in force according to special laws, presidential decrees, and resolutions and directives of the Cabinet of Ministers.

During the considered period of time the number of tax privileges increased as follows:

- By changes in the Law "On the VAT" dated May 6, 1999 taxation of critical imports at a zero rate was prolonged till January 1, 2001. Though the list of critical imports was shortened from 127 to 49 products, the very fact that such a privilege exists creates a danger of the list undergoing constant enlargement.
- 9 special (free) economic zones were created and priority development areas were determined in 7 oblasts and Crimea, where entities are granted privileges on VAT, income tax, and land fees.
- According to the concluding provisions of the Law "On the fixed agricultural tax", agricultural producers are exempted from payment of the fixed tax from January 1, 1999 till January 1, 2001; pursuant to the Presidential Decree "On supporting agricultural producers" they are exempted from the VAT for the period from January 1, 1999 till January 1, 2004.
- The Law "On conducting an economic experiment at enterprises of Ukraine's mining and metallurgy sector" dated July 14, 1999 established a profit tax rate at the level of 30% of the rate currently in force for some en-

terprises of the sector, starting from July 1, 1999 till January 1, 2002.

- In accordance with a change to the Law "On the VAT" dated July 7, 1999 the VAT is not imposed on sales of vacation packages for sanatoriums and health centers in Crimea.
- In accordance with a change to the Law "On the VAT" dated July 14, 1999 VAT is not imposed on housing construction from January 1, 2000 regardless of the sources of financing[13].
- Tax arrears of the coal-mining sector, sugar refineries, agricultural enterprises, and water transport enterprises were written off or restructured in accordance with various laws and presidential decrees.

Additional taxes and levies

Continuous budget imbalances lead to the introduction of additional taxes and levies, which restrain business and investment activity.

Continuous budget imbalances have led to the government introduction of additional taxes and levies for the purpose of quick increases in budget revenues. Such actions restrain business and investment activity since they cause increases in the tax burden and expenditures on tax calculating and accounting.

According to the Law of Ukraine "On amending the Law of Ukraine 'On the taxation of enterprise profit'" dated April 6, 1999, one of these unjustified taxes was abolished, i.e., the 10% amortisation deductions to the state budget. The same law increased the reduction coefficient for calculating the amortisation from 0.6 to 0.8. Together these two actions diminished the profit tax burden, while increasing the investment resources of enterprises.

On the other hand, some acts introducing new taxes and levies were adopted during the year: the Law of Ukraine "On the levy for development of viticulture, horticulture, and hop-growing" dated April 9, 1999, the Presidential Decree "On the stamp duty"[14], and the Cabinet of Ministers Resolu-

[13] According to the previous edition of the law, VAT was not imposed on housing construction for individuals financed by themselves, as well as the transfer of title of said housing.

[14] The decree was revoked since the Law of Ukraine "On the stamp duty" was adopted.

tion "On introducing the system of gathering, sorting, transportation, processing, and utilisation of used packages (packaging)"[15]. Moreover, some changes were made to the Law "On the levy for mandatory state pension insurance". In accordance with the changes, the basis for calculating the levy for mandatory state pension insurance was enlarged to include operations on currency sales/buying, jewelry sales, transfer of ownership of cars, production and import of tobacco goods, real estate acquisitions, and cellular mobile telecommunication services[16].

Guidelines for the development of tax legislation

The future development of tax legislation should envisage incentives for business and investment activity, as well as create conditions for steady economic growth. These problems are to be solved by the Tax Code.

The future development of tax legislation should fulfill the main purpose of tax policy–to determine incentives for business and investment activity, as well as create conditions for steady economic growth. The improvement of tax legislation should be aimed at decreasing taxpayer expenditures and achieving equal distribution of the tax burden. These problems are to be solved by the Tax Code of Ukraine.

Four drafts of the Tax Code have been submitted to the Verkhovna Rada. Two of them propose to replace the VAT and profit tax with sales tax. Although, the replacement of two taxes with one simplifies the system of charging and accounting, the sales tax may lead to distortions in the incentives for economic activity.

Introduction of the sales tax will not help to foster competition in Ukraine. If the tax is introduced, in order to evade it producers will agree to mergers with monopolistic resource suppliers. Consequently, the latter will extend their monopoly on the market of final goods.

The requirement to pay the sales tax on the day when the obligation appears, as envisaged by one of the drafts, will deprive economic entities of flexibility in planning their cash flows. Every buyer (taxpayer) will be forced to have reserve funds in case a tax obligation unexpectedly occurs (e.g.,

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[15] The resolution established tariffs for gathering, sorting, transportation, processing, and utilization of used packages. It was cancelled by the Presidential decree dated July 22, 1999.

[16] The changes were made by the laws of Ukraine dated October 22, 1998 and July 15, 1999.

shipment of products from a supplier). Moreover, this requirement in fact establishes the priority of tax payment over settling with suppliers.

Finally, introduction of the sales tax does not jibe with Ukraine's intentions to integrate into the European Union. Rejection of the value-added and profit tax while introducing the sales tax instead will hinder the harmonisation process of Ukrainian economic legislation and that of EU countries. As a result, resolution of the double taxation problem will be complicated, which in its turn will restrain foreign investment.

Foreign trade

We consider the lack of well-defined development priorities for the foreign trade sector to be a major problem of foreign economic activity regulation. It has not been conclusively defined which path Ukraine will take–protectionism or free trade. On the one hand, Ukraine has many restrictions for conducting normal trade, and state bodies are continuing to use administrative methods to control business activity. On the other hand, Ukraine aims at joining international agreements that will let it strengthen its positions in external markets, though these agreements stipulate a non-discriminative trade regime. That is why laws adopted during the last year have been contradictory: some establish import or export barriers (a direct demonstration of protectionism on behalf of the state), while others abolish restrictions and foster free trade.

Import regulation

Frequent changes in import duty rates significantly complicate import activities of enterprises.

Frequent changes in import duties (during 1998–1999 over 40 normative-legal documents were adopted that changed import duties) significantly complicate import activities of enterprises. The indefiniteness of the legislation is exacerbated by the existence of several authorities that are eligible to set duty rates. During the last year import duty rates changed according to laws approved by the Verkhovna Rada, as well as by Cabinet of Ministers resolutions. This practice was extended in the Law of Ukraine dated October 14, 1998 "On the procedure for setting tax and duty rates (obligatory payments), other elements of tax bases, and tax privileges", which enabled the Cabinet of Ministers to change import duty rates for the majority of goods until the issue of the Single Customs Tariff is resolved.

The Law "On the implementation of special measures regarding imports to Ukraine" threatens sound competition and normal trade.

The Law "On the implementation of special measures regarding imports to Ukraine" dated December 22, 1998 threatens sound competition and normal trade. This Law enables all enterprises to apply to plenipotentiary state authorities for implementation of special measures regarding imports if their increase threatens "significant harm to domestic producers". Some enterprises have already applied

to the Interagency Committee for Foreign Trade, requesting special measures regarding certain import goods[17].

Ukraine is gradually abandoning the method of regulating imports via minimum customs value.

At the same time, progressive changes have taken place in import regulation during the last year. Particularly, Ukraine is gradually abandoning the method of import regulation by minimum customs value. Cancellation of the minimum custom value for certain groups of products significantly reinforces competition between foreign and domestic producers. The most important step in this direction was the Cabinet of Ministers resolution dated July 29, 1999 "On amending certain resolutions of the Cabinet of Ministers of Ukraine on setting the minimum customs values for light industry and agricultural products". The decree enables importers to set customs values independently, particularly for all grains, groats, flour, meat, butter, cheese, margarine, vegetables, fruits, nuts, jams, juices, etc. The minimum customs value was also cancelled for some goods of the light industry–coats, mackintoshes, jackets, tights, coverlets–and also excisable goods–coffee and chocolate.

Export regulation

In 1999, two laws were adopted that significantly limit the exports of some goods from Ukraine. They were an important victory for politicians who consider protectionism and foreign trade restrictions as a tool for achieving economic growth.

The laws "On scrap metals" and "On the rates of export duties for the seeds of some oil crops" significantly limit the exports of some goods from Ukraine.

The Law "On scrap metal" dated May 5, 1999 envisages establishment of an export quota for ferrous scrap metal, and a full ban on non-ferrous scrap metal exports.

The Law "On the rates of export duties for the seeds of some oil crops" dated September 10, 1999 sets a 23% duty on sunflower seeds. This law is an attempt to artificially ensure sup-

[17] The Interagency Committee for Foreign Trade has already handled a claim of the Iskra open joint-stock company on instigating and conducting a special investigation concerning imports of electric lamps to Ukraine, as well as a claim of the Fake Fur Factory open joint-stock company concerning imports of fake fur and pile fabric to Ukraine. The Committee made a decision to limit lamp imports, though, according to the "List of monopolist-enterprises in the national market(as of 01.01.99)", the Iskra open joint-stock company is a monopolist.

plies of seeds to oil-extraction plants by making exports unprofitable.

The adoption of these laws will hit not only trader-exporters but also scrap metal collectors and seed producers, since the domestic prices of scrap metal and seeds will drop resulting from the increased supply. Consequently, sunflower production and scrap metal collecting will decrease next year.

Further ways of solving the problem

Liberalisation of the Law "On foreign economic activity" may essentially limit state interference in enterprise activities in the sphere of foreign trade.

Changes to the Law "On foreign economic activity" proposed by a group of people's deputies may essentially limit state interference in enterprise activities in the sphere of foreign trade. If these changes are approved, foreign economic activity will only be able to be prohibited judicially, for a period not exceeding half a year, and only for violations in said activity. Currently the Ministry of Foreign Economic Relations and Trade is eligible to stop the enterprise activities temporarily (the term is not defined precisely) "in cases when the activity may hamper the interests of national economic security". But since the term "national economic security" is very indistinct, the state has the unlimited right to interfere in enterprise activities.

Transformation of the customs tariff system of Ukraine according to the GATT/WTO system is an important component of changes needed in legislation.

One of the priorities of state policy on foreign trade is the preparation for Ukraine's entry into GATT/WTO. That is why transformation of the customs tariff system of Ukraine according to the GATT/WTO system is of particular importance. Therefore, a law "On the single customs tariff" needs to be adopted that will establish European methods for evaluating the customs value of goods. The guidelines for reforming legislation on foreign trade should also include non-discrimination and a national regime in the sphere of import taxation (calculating VAT, excise, and other levies), as well as harmonization of state support of some sectors according to GATT/WTO requirements.

Foreign investment

During the last year the government has taken steps to attract foreign investment. These measures provide for regulation of the special relationship with investors (product sharing, concessions). However, an integrated policy focused on the improvement of the investment environment was not developed. That is why, alongside granting privileges, there are still requirements which restrict investor freedom to take decisions or which cancel guarantees and benefits adopted earlier

During the last year, in the field of investment activity regulation the following changes were implemented:

- relations concerning product sharing of extracted underground resources throughout Ukraine were adjusted;
- terms of concessions of state and communal property were determined.

The Law "On product sharing" dated September 14, 1999 regulates relations regarding the process of drafting, execution, and expiry of agreements on product sharing.

The Law "On product sharing" dated September 14, 1999 will have a significant impact on the investment climate in Ukraine. This law regulates relationships regarding the process of drafting, execution, and expiry of agreements on product sharing. According to these agreements, Ukraine charges investors for searching, prospecting, and extracting mineral resources at a determined site of underground resources; and the investor is responsible for fulfilling assigned operations at its own cost and risk, with further expense compensation and profit in the form of a share of the product.

The law creates the following conditions and benefits for investors:

- The agreement on product sharing is signed with the winner of a tender, held according to lawful procedure and creating equal starting conditions for all potential investors.
- Regarding parties' rights and responsibilities determined by the agreement on product sharing, the state guarantees application of the laws currently in effect on the date of the agreement, for the whole term. This regulation considerably reduces investor risks.
- Investors are not subject to normative and legal acts of executive and local authorities if these acts restrict investors' rights as determined by the agreement on product

sharing, with the exception of orders of state bodies controlling and supervising underground resources usage.

- The state rejection of judicial immunity, immunity from preliminary subpoena, and court decision execution is provided in agreements on product sharing drafted with the investor's participation.
- Requisitioning from bank accounts opened by investors throughout Ukraine for servicing activities defined by the agreement on product sharing cannot be made without acceptance.
- Job placement of foreigners employed by investors in Ukraine, within the limits and professions determined by the agreements on product sharing, can be done without seeking permission to hire.

On the other side, the law establishes norms restricting investor activity freedom, and investment attractiveness as well. The law defines that the agreements on product sharing should address the following investor responsibilities:

- preference to Ukrainian products, work, and services under equal terms of price, schedule time, quality, and compliance with international standards;
- employment predominantly of Ukrainian citizens throughout Ukraine for carrying out jobs determined by the agreement.

The Law of Ukraine "On concessions" defines the concession of state and communal property, and terms and procedures of its fulfillment.

The Law of Ukraine "On concessions" dated July 16, 1999 is another important framework law. The law defines the meaning of a concession[18] of state or communal property, and terms and procedure of its fulfillment. The law specifies a list of fields of economic activities of state enterprises able to be provided at a concession. The list is long and contains sectors which are attractive for investment, in particular municipal infrastructure sectors.

The Cabinet of Ministers approves the list, while decisions on the concessions are made on basis of concession competitions. Thus, the law creates new opportunities for investment activity, depending on government actions.

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[18] According to the law, a concession is the right to the construction and/or running of a concession granted to business entities by authorised executive or local authorities on a paying basis for a fixed period.

The problem of instability of legislation on foreign investment remains uncorrected for the past year.

Instability of legislation on foreign investment remains a problem that was not overcome within the last year. The Verkhovna Rada approved a resolution "On amending the Resolution of the Verkhovna Rada of Ukraine 'On the procedure of implementing the Law of Ukraine 'On the regime of foreign investment'" dated July 6, 1999. According to this act, the provisions of the above law and other acts of special legislation of Ukraine–in particular on tax, custom, and investment, being current on the date of investment registration–will be applied to foreign investments that were actually implemented and registered within the terms of the Law "On foreign investment" dated March 13, 1992 and for 10 years from the date of investment registration, at the foreign investor's request.

This decision of the Verkhovna Rada resolves the matter regarding tax benefits of enterprises with foreign investment, that were imposed in favour of these enterprises within the terms of the Law "On foreign investment". But the President submitted an appeal about the unconstitutionality of the resolution dated July 6, 1999 to the Constitutional Court. By a resolution dated July 14 the Cabinet of Ministers stipulated that until the Constitutional Court decision the disputed enterprises should be taxed on a standard basis. However, the Cabinet of Ministers abolished this resolution on August 18.

Special economic zones

Inconsistency and opacity of the state policy for attracting foreign investments at the central level have led to the situation where solutions to this problem have been initiated in particular regions via creating special economic zones (SEZ). During the last year 9 SEZ were created. In 7 oblasts and Crimea special regimes for investment activity were established within priority development areas (PDA)[19]. In the near future it is planned to establish at least one more SEZ – "Reni" (within the Reni port on the Danube). The special regimes for investment activity, which are in force on the territory of SEZ and PDA, envisage granting tax and customs privileges to economic entities of the zone[20]. In order to obtain SEA or PDA status enterprises should carry out an investment project in a priority field of the economy within the territory of the zone, as well as sign a contract and register with bodies which control the zone's activity. But there are a number of problems connected with non-transparent and unclear regulation of activities within the SEZ.

Entering procedure

The mechanism for obtaining the status of a SEZ or PDA entity is gradually becoming more and more complicated. The high volume of investments necessary to enter a zone gives superiority to large investors.

Analysis of laws and decrees on special economic zones and priority development areas issued during the last year indicates a gradual complication of the mechanism for obtaining the status of SEZ or PDA entity. Thus, for example in "Zakarpattia", which is the first SEZ created during the mentioned period (Presidential Decree dated December 9, 1998), in order to receive the status of a zone entity it was only necessary to perform an investment project and register. In the following decree dated December 18, 1998 "On the special regime for investment activity in priority development areas of Luhansk oblast" and in the Law dated December 24, 1998 "On the SEZ and the special regime for investment activity in Donetsk oblast" this norm remained, but now only those enterprises having investments in the amount equivalent to at least $1 million were exempted from profit

[19] SEZ and PDA were created for periods of from 15 to 60 years according to the Law "On the general principles of creation and functioning of special (free) economic zones" dated October 13, 1992.

[20] The advantages and drawbacks of the existence and granting of tax and customs privileges are not analysed here.

taxation. The Law dated December 24, 1998 "On the special regime for investment activity in Transcarpathia oblast" envisages similar norms, except for the volume of an investment project necessary for the enterprise to be granted profit tax privileges (at least $250 thousand). Further, all the subsequent decrees and laws on the creation of SEZ or PDA (except the "Interport Kovel" SEZ and the PDA in Volyn oblast) contain restrictions concerning the amount of investments necessary to obtain the status of the SEZ entity and be granted the privileges.

The high volume of investments necessary to enter the zone indicates that preferences are given to large investors. This means that there will not be many entities in the zone, and thus local authorities will be able to control and put pressure upon them.

Moreover, according to a presidential decree dated May 17, 1999 the Agency on Special (Free) Economic Zones was established. Its declared goal is to ensure the realisation of state policy on creation and functioning of special/free economic zones. The agency was granted many authorisations which cross those of local bodies. For instance, the agency's reconciliation and approval of all investment projects conducted within the SEZ or PDA will only exaggerate the unclear procedure for obtaining the status of zone entity. In addition, it is unknown how the agency will reconcile its actions with local authorities. The appearance of the agency is direct evidence of the opposition between central and local authorities. For central authorities this way of controlling SEZ activity is an attempt to counterbalance the broadening of local bodies' authorities concerning influence in their area.

Exiting procedure

None of the examined legislative acts regulates the procedure for exiting the zone.

None of the examined legislative acts contains an indication of the grounds for registration cancellation or contract voiding on behalf of the authority that registered or made a contract with the zone entity. Mostly, contract settlement and registration are done by different authorities. The mechanism for their cooperation and responsibility to zone entities are not defined. Thus, all these authorities will be able to set conditions for zone entities, threatening cancellation of their status, which, in its turn, will deprive the entities of their privileges.

Ongoing activities

The main incentive for enterprises to obtain the status of SEZ entity is in its numerous tax privileges. At the same time, stability of the privileges is not guaranteed, but the extent of reporting and inspections for zone entities is much larger.

The main incentive for enterprises to obtain the status of SEZ entity is the existence of numerous tax privileges. Here some indefinite points should be indicated.

- Firstly, the stability of the tax privileges is not guaranteed. Every legislative act on SEZ contains a norm on the delegation of authority to the Cabinet of Ministers concerning determining the priority fields of activity and lists of raw materials (inputs) which are subject to import privileges. Thus, there is a danger that these lists will be altered every time the Cabinet of Ministers changes (during the 8 years of independence of Ukraine it happened 6 times).

- Secondly, all legislative acts contain a norm according to which SEZ entities should submit to the State Tax Administration a monthly report on utilisation of raw materials, goods, and accessories on which no duty or VAT were imposed while coming in. Only SEZ entities are required to do this.

Since the procedures for entering/exiting and regulation of zone entity activities are not transparent, a competitive environment will not develop within the SEZ. A number of entities engaged in a certain activity will obtain monopolistic rent in the form of tax privileges, accompanied by the interference of local and central authorities.

At the same time, privileges on new equipment coming in to contribute to the creation of modern enterprises within the zone. The rent available at these enterprises will encourage other enterprises to improve, in order to survive in the competitive environment, or to seek rent, too.

Further ways to resolve the problem

Improvement in the conditions for business activity within the SEZ and PDA is possible only under the stipulation of corresponding changes in legislation. In order to achieve this it is necessary to:

- within the framework of the Law "On the general principles of creation and functioning of special (free) economic zones" clearly describe the authorisations and responsibility of the bodies which are entitled to interfere in activities of SEZ (PDA) entities;

- decrease restrictions concerning the amount of investments necessary to obtain the status of SEZ (PDA) entity, fostering development of competition within the zone and limiting interference of the authorities in zone entity activities;
- clearly describe the procedures for obtaining and cancellation of the SEZ (PDA) entity status either in the abovementioned law or in each legislative act on creation of an SEZ (PDA);
- review the "Regulations on the Agency for Special (Free) Economic Zones", aiming at more precise defining of the agency's authorisations. While doing so, the norm according to which the agency has the right to reconcile and approve every investment project realized within an SEZ (PDA) should be abolished. Firstly, it will allow to avoid discrepancies between local and central authorities; secondly, it will reduce the conditions for SEZ entity registration.

Contract enforcement

One of the major risks while conducting business in Ukraine is non-fulfillment of contracts. In 1992 the Law of Ukraine "On ownership" was adopted. It established the right of private ownership and envisaged the possibility of its assignation. But in the Law "On bankruptcy" dated May 14, 1992 the mechanism for assignation of ownership rights was not described clearly. Consequently, failure to execute business agreements on behalf of contractors has become a mass phenomenon

Law on bankruptcy

During the last year some important steps have been made in order to improve the mechanism for assignation of property rights. The most important step is creation of an effective bankruptcy procedure, which is regulated by the Law "On amending the Law of Ukraine 'On bankruptcy'".

During the last year some important steps have been made in order to improve the mechanism for assignation of property rights and remove barriers which have blocked its action.

The most important step is creation of an effective bankruptcy procedure, which is regulated by the Law "On amending the Law of Ukraine 'On bankruptcy'" dated June 30, 1999.

All lenders can be conditionally divided into three groups, depending on the guarantees of their claims and interest in the debtor's future. In the first group are lenders whose claims are ensured with a pledge; they are protected best of all. According to the law, they may raise property claims to their debtor even when the proceeds obtained from sale of the pledge were insufficient for complete claims settlement.

The second group includes the lenders whose claims are ensured with business agreements. Claims of the lenders ascribed to this group may be quickly satisfied only in the case when the promissory note is negotiated to a third party[21]. It is difficult to obtain debt repayment since such claims are satisfied in the fourth turn[22] after the complete fulfillment of the

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[21] Development of factoring activity in the promissory notes market will become a positive consequence of creating a strict mechanism for transfer of ownership. After all, in such circumstances this activity will become less risky. Lenders will be able to satisfy their claims quickly through the sale of corresponding liabilities.

[22] First, the claims ensured with a pledge are satisfied; second, the claims which appeared from liabilities to employees of the

previous claims. Thus, the risk exists that not all lenders will manage to obtain full debt repayment (because of the low liquidity of many enterprises, and existence of large tax and wage arrears).

The third group of lenders includes potential investors, who find the norms of the law to be very convenient. After the bankruptcy case is processed, relations (including those between the enterprise and the investor) can be regulated through setting up a peace pact. Thus, having bought up the enterprise's liabilities it is easy for the investor to become its competent owner on beneficial terms. This scheme has the following advantages:

- A peace pact may envisage the exchange of the debtor's liabilities for its shares. If majority shares are passed to the lender in such a way he can quickly reorganize the enterprise according to the own needs.
- If a peace pact is set up, tax authorities are supposed to agree to write off the entire tax indebtedness for the previous two years. According to the general procedure, if debtor's assets are sold, the claims on tax and levy payments are satisfied before those of lenders not ensured with a pledge. Thus, a lender appearing as an investor while entering into a peace pact obtains a relatively larger part of the debtor's property due to the latter's tax arrears write-offs.
- While conducting reorganization there are no restrictions as to the number of employees that should remain at the enterprise. In case of reorganization or setting up a peace pact this number is determined in the reorganization plan.
- When using this way to purchase an enterprise, the investor saves money and time compared to other ways.

Thus, according to the new law the most prospective enterprises among present debtors will change owners and will manage to become efficient. All others, which are of no interest to investors, should be liquidated. But taking into account the long terms for reorganization and liquidation de-

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bankrupt enterprise; and third, claims on tax and levy payments. Claims of lenders not ensured with a pledge are fulfilled in the fourth turn.

termined by the law (about 3 years in general), one should not expect a bankruptcy deluge.

There is another positive aspect of the law: central executive authorities and local authorities are obliged to implement measures for avoiding bankruptcy of the debtor enterprise. Thus, if authorities' activities have led or potentially can lead to bankruptcy of the enterprise, it has the right to appeal such activity in the court as being illegal. Unfortunately, tax authorities were not mentioned in this norm, though their activity may cause significant losses to enterprises, leading to their protracted insolvency.

In accordance with the new law, enterprises which deliberately accumulate arrears trying to recoup their losses will face the substantial threat of asset liability. After reorganization or liquidation of such enterprises through the bankruptcy procedure, firstly the competitive environment will be improved, and secondly enterprises will be motivated to strict fulfillment of their debt liabilities.

At the same time, the law is ambigous concerning bankruptcy of city-maintained enterprises and those where the share of state ownership exceeds 25%. The bankruptcy procedure of such enterprises will be delayed since their liquidation will aggravate societal problems resulting from an increase in unemployment.

Court decision enforcement

During the period of 1998–1999 the system for execution of court decisions has become stricter.

A strict system for execution of court decisions is a precondition for the efficient functioning of the ownership rights assignation mechanism. During the period of 1998–1999 positive changes have been made in the system:

- According to the Law "On the state executor service" dated March 24, 1998 the function of executing court decisions was transmitted to state executors who are independent of the court. Whereas earlier it had been a direct function of the court, with decisions made by the court were executed by its officers. Delivering the court from such unnatural duties will allow more impartial decision making. Besides this, the existence of a strict activity scheme for state executors will contribute to the quick execution of court decisions on debt collection.

- The Law "On executor enforcement" dated April 21, 1999 regulates the conditions and procedure for enforcing court and other bodies' decisions.

Thus, an effective bankruptcy procedure, combined with a strict mechanism for court decision execution, will increase payment discipline and considerably reduce the risk of contract failure.

Payment system

Imperfections of the payment system blocked the functioning of the mechanism for property assignation. The Presidential decree "On the procedure for collecting debts of taxpayers to budgets and state target funds" and joining the Geneva Conventions of 1930 on Bills of Exchange contributed to removing some of them.

During the last year the payment system has been improved substantially. Its imperfections blocked the functioning of the mechanism for property assignation.

The Presidential Decree "On the procedure for collecting taxpayer debts to budgets and state target funds" dated June 28, 1999 cancelled extrajudicial fund seizure from the accounts of enterprises with tax arrears. Instead of seizure without acceptance, asset liability was introduced. It envisages the sale of debtor's assets in case of failure to collect debts to the budget and state target funds in the required time.

The major consequences of the decree are:

- Possibility for both debtors and lenders to plan cash flows on their accounts lucidly. According to the procedure for seizure without acceptance, the debtor was often unable to settle liabilities in time and in full, since all cash that arose on the account was seized for the redemption of tax and levy arrears. Moreover, if one enterprise owed another while the latter had tax debts, the tax authorities had the right to seize funds from the account of their debtor's debtor.

- Debtors are no longer able to ignore account payables while deliberately accumulating arrears on the blocked account. The threat of asset liability to the state frightens more than to the private creditor. Thus, we should expect an increase in payment discipline.

Joining the Geneva Conventions of 1930 on Bills of Exchange (laws of Ukraine dated July 6, 1999) is of great importance for the development of civilized mechanisms for nonmonetary settlements. The main presumable consequence is unification of bill of exchange settlements. This will enable

using bills or promissory notes as a universal secured means of payment in the environment of a de-monetized economy[23].

Further ways of solving the problem

Further steps in order to create the conditions for exact fulfillment of commitments on behalf of contractors should include:

- improving the norms in the Decree "On the procedure for collecting taxpayers' debts to budgets and state target funds"; particularly while selling the assets of tax debtor enterprises, the concerns of other lenders should be considered;
- developing strict procedures for the responsibility of state enterprises and those enterprises where the share of state property exceeds 25%;
- harmonization of Ukrainian legislation on bills of exchange in accordance with the Geneva Conventions;
- developing strict legally determined conditions for factoring activity.

[23] Previously, a series of special regulations was adopted for the bills of every significant issuer.

Privatisation and the stock market

Privatisation in Ukraine has reached one of the most difficult stages–the cash sale of major enterprises and monopolies. This requires elaboration of individual privatisation procedures. The existence of large-scale internal and external debts requires the quick sale of state property at a maximum price. At the same time, entering the most difficult privatisation stage coincides with aggravating state interference in the economy and increasing political instability. These in turn can lead to wholesale prohibition of privatisation in Ukraine and the beginning of re-privatisation. Under such conditions privatisation needs strict legislative underpinnings, which would guarantee the irrevocability of the process, protect investors from unjustified re-privatisation, and ensure participation of strategic investors in the sale of major Ukrainian enterprises. The laws on privatisation in certain sectors and monopolies should be of particular importance. Land resources need to be included in the privatisation process as well. The other side of the problem is enterprise post-privatisation existence in the stock market. The stock market in Ukraine does not yet perform its functions for ensuring fast capital flows, property rights transition and protection, or attraction of investments. The legislation on these issues is not complete and in many cases is not clarified in bylaws

State Privatisation Program

The main legislative document in the privatisation sphere adopted this year is the Presidential Decree "On the State Privatisation Program".

The main legislative document in the privatisation sphere adopted this year is the Presidential Decree "On the State Privatisation Program", dated February 24, 1999. The initial version of the decree (dated December 30, 1998) envisaged two important changes: the possibility of privatisation by means of increasing the statutory fund, and using state bonds as payment for shares. The former modification should have facilitated the participation of strategic investors in privatisation (currently Ukraine lacks the mechanism for investments to be applied during privatisation that would be favorable for investors). The latter modification should have partially resolved the problem of state indebtedness. But the deputies did not agree with the proposals, thus in the second edition of the decree the President had to delete the corresponding clauses.

In the initial version of the decree some important measures for shareholder rights protection were proposed by the

President. It was envisaged that while conducting additional share emissions, public corporations' shareholders will have prevailing rights to purchase extra shares in the amount proportionate to their share in the statutory fund at the point of the emission decision. Subscription to additional shares was proposed to be conducted in two equal stages. At the first stage shareholders would realize their first-priority right to purchase additional shares, and at the second other investors would make subscriptions.

The norm on minority shareholder protection was introduced in Ukrainian legislation for the first time. According to it, if a shareholder did not participate in the gathering which approved a decision on statutory fund changing, or voted against the decision, the issuer would be obliged to offer the shareholder a chance to redeem his shares at a price which is not lower than nominal. Though this norm could block some necessary decisions on a company's reorganisation (not all companies have free funds for share redemption), in general it was rather progressive.

Nevertheless, the deputies rejected all these proposals. In the final version of the decree only one norm was retained. In accordance with it, a public company founded through privatisation is obliged to redeem shares from shareholders at their request at a balance price, if those shareholders voted against the decisions on the purchase or alienation of the public company's property, which cost exceeds 25% of the company's statutory fund.

Though the main initiatives were blocked, some progressive issues still remained in the decree:

- Privatisation plans can now envisage only the remainder of strategic enterprises' shares under state ownership and only in the amount of 25% or 50% plus one share.
- The rules of competitions were changed. Finally, a competition is allowed to be held even in the case of one application (previously the minimum number was two, thus investors had to create fictitious firms). From now on the applicant need only agree to all sales terms defined by the State Property Fund. However, the by-laws that would ensure fulfillment of the norm have not been adopted yet.
- From now on the terms of competition for strategic enterprises' majority holding sales should envisage

banning the participation of those economic entities which conceal information about their real owners.

Later, in summer 1999, the President tried to change the privatisation program's clause which permits beginning bankruptcy cases only after the privatisation end (share allocation plan's fulfillment). In the decree dated June 27, 1999 the President proposed to allow bankruptcy procedures for enterprises privatised by more than 75%. This would bury the "dead" situations in which many enterprises find themselves now: there is no demand for their shares because in fact those enterprises are bankrupt. At the same time, they are not eligible for the bankruptcy procedure (another way to change ownership for more efficient one). But the deputies rejected this amendment.

Privatisation in some sectors

The Presidential Decree rejected by the Verkhovna Rada "On privatisation peculiarities of the Ukrtelekom Ukrainian state telecommunication company" dated June 28, 1999 was the most important among the legislative acts that determine privatisation in some sectors and enterprises.

The Presidential decree "On privatisation peculiarities of the Ukrtelekom Ukrainian state telecommunication company" was rejected by the Verkhovna Rada. The Presidential Decree "On some issues of privatisation in the power sector" did not envisage any changes in legislation, thus it was not considered by the Verkhovna Rada; it was not a document of direct action.

According to the decree, 50% plus one share of the Ukrainian local telecommunications monopolist's statutory fund would remain under state ownership. Another part of shares would go to privileged subscription, and the remainder would be proposed to strategic investors. The decree emphasised the obligatory engagement of advisors on a competitive basis and an Ukrtelekom audit inspection. A strategic investor would be offered a share holding in the amount of not less than 25% plus one share in an open cash auction. The decree defined a strategic investor to be "a legal person operating in telecommunications and having internationally-acknowledged authority as well as experience in the telecommunications market".

After the crucial decree was rejected, the Presidential Decree dated May 28, 1999 "On changes to the Presidential Decree dated June 15, 1993" became the only improvement concerning the privatization of Ukrtelekom; it permitted the corporatization of Ukrtelekom and Ukrposhta.

The Presidential Decree "On some issues of privatisation in the power sector", dated August 2, 1999, did not envisage any changes in legislation; thus, it was not considered by the Verkhovna Rada. But because of this, instead of having a

document which would regulate power company privatisation in detail, a political declaration was adopted on executive authorities' readiness to resume power sector sales to strategic investors after more than a year's hiatus.

Again the decree defined power companies' stock purchasers to be persons that have experience in power sector administration and activities in the power market. In addition, the competition terms approved by special resolutions of the Cabinet of Ministers may determine the forms and mechanisms for investment depositing, as well as the government obligations to foster companies' indebtedness restructuring, and power tariffs. Moreover, the competition terms may envisage transmission of the state stock holding (or its part) into the competition winner's disposal.

The most important issue in the decree was the approval of the privatisation scheme with advisor participation. Power company sales through international mediators reduces political pressure on the privatisation process, which did not allow to attract strategic investors during initial competitions for power sector stock holdings sales.

Privatisation of unfinished construction projects

The Presidential decree "On the peculiarities of privatisation of unfinished construction projects" removed a number of problems which prevented acceleration of such privatisation.

The Presidential Decree "On the peculiarities of privatisation of unfinished construction projects", dated May 28, 1999, did not provoke any objections on behalf of the Verkhovna Rada and came into effect, removing a number of problems which prevented acceleration of such privatisation.

Purchasers of unfinished construction projects will have considerable privileges. Firstly, after 50% of the project's cost is paid (30% for unfinished housing projects) a postponement in payment can be granted for a period of 5 years (10 years for unfinished housing projects) with the interest rate tied to inflation. Secondly, privatisation of unfinished construction projects is not subject to taxation. Thirdly, during the construction period, determined by privatisation terms, purchasers are permitted to include costs related to construction as gross expenditures while counting income tax. Fourthly, purchasers of unfinished construction projects are exempted from land payments for the construction period.

According to the new document, purchasers (except foreigners) may buy land allotted for the construction together

with the unfinished construction projects. Selling of unfinished construction projects for demolition is also permitted.

Land privatisation

The Presidential Decree "On non-agricultural land sales" regulates the procedure for privatisation of land, occupied by privatised enterprises. This is the first step towards a Ukrainian land market.

The Presidential decree "On non-agricultural land sales", dated January 19, 1999, has also came into effect. The decree regulates the procedure for privatisation of land occupied by privatised enterprises. This is the first and very important step towards a Ukrainian land market; 50 thousand plots have been privatised in Ukraine without regulation of land property issues.

The document defines the lands which can be subject to sales-purchases and settlements, as well as the procedure for their assessment. The document determines that land sellers are local authorities in case of municipal property and state administrations in case of state property. Purchasers are economic entities registered in Ukraine that own real estate which is located on this land.

State corporate rights management

The National Agency of Ukraine for State Corporate Rights Management was created according to Presidential Decree. By its very nature, this state institution is interested in state property expansion and hindering privatisation.

The National Agency of Ukraine for State Corporate Rights Management was created according to the Presidential Decree dated July 7, 1998. On September 2, 1998 another Presidential Decree approved the Regulations of the agency.

According to the President's decision, the function of state corporate rights management was transferred from the State Property Fund (which remains the owner) to the new agency. Thus, another state institution has appeared that is by its very nature interested in state property expansion and hindering privatisation.

The agency's main duty is to hold competitions to determine authorised persons for state rights management. The conditions for transfer of state corporate rights management and responsibility for the results of management are very different for executive bodies and legal entities. Thus, the terms of competition for state property management are unequal.

The problem of opposition between state management and privatisation should be resolved by the law on management of state property (currently the draft is being considered by the Verkhovna Rada). Its second edition provides the National Agency with considerable rights. For instance, the agency will have the right to prepare proposals for the gov-

ernment on state corporate rights alienation (i.e., sale) without the agreement of the State Property Fund. It will also be able to independently organise competitions to appoint authorised persons. Taking into consideration the importance of privatisation as grounds for efficient enterprise management, the agency's rights need to be diminished to limit the possibilities of its interference in the privatisation process.

Taxation of stock market operations

The Presidential decrees "On taxation of operations in the Ukrainian securities market" and "On fostering the development of the stock market in Ukraine" were aimed at softening the tax burden of the stock market, but the Verkhovna Rada rejected these documents. At the same time it had to respond to the problem through approving some changes to the laws on the VAT and the profit tax.

The Ukrainian securities market found itself enchained with taxes in autumn 1997 after the adoption of new laws on business profit taxation and the value-added tax.

According to the law on profit taxation,a 30% tax was imposed on joint-investing funds obtained from placing investment certificates. This led to an immediate reduction in market operators' activities. According to data available from the State Committee for Securities and the Stock Market, at the beginning of 1998 the overall value of registered investment certificates issues accounted for 1,471 million hryvnias, while during 1998 the amount of new emissions made up only 4 million hryvnias.

A tax was also imposed on the proceeds obtained by companies from issuing corporate bonds. In the first half of 1997 the overall amount of registered corporate bonds emissions accounted for 102 million hryvnias, while for the whole of 1998 it made up only 6 million hryvnias.

In addition, double taxation was introduced for dividends obtained by non-residents in case of their repatriation. At the same time, resident professional securities traders who had this business as their sole occupation fell under the general rules for tax reporting on securities operations, which involved significant administrative overhead. Moreover, VAT was imposed on their services.

Solutions to these problems were proposed by the Presidential decrees "On the taxation of operations in the Ukrainian securities market" and "On fostering the development of the stock market in Ukraine" (both dated June 4, 1999). But the Verkhovna Rada rejected these documents. At the same time, it had to respond to the problem, so it approved some changes to the laws on VAT and profit taxation (the Law "On changes to some laws of Ukraine aimed at stimulating investment activities", dated June 15, 1999). Dividends ob-

tained by non-residents were exempted from the profit tax (repatriation tax still remained). Non-residents were also granted the right to bring in capital assets as contributions to statutory funds without paying VAT. Investment funds and companies also obtained small tax concessions.

Stock market infrastructure

By the Decree "On general functioning principles of the National Depository of Ukraine ", dated June 22, 1999, the President hastened the development of the National Depositary System and the introduction of non-documentary securities.

By the Decree "On general functioning principles of the National Depository of Ukraine", dated June, 22 1999, the President ended a conflict between the project to establish a National Depository and the project for a non-governmental depository, which is financed by USAID. The Ukrainian stock market obtained a central depository institution, which will hasten the development of a National Depository System and introduction of non-documentary securities.

The Law of Ukraine "On the membership of securities market professionals in self-regulating organisations", dated June 27, 1999, fixed the norm introduced several years earlier on obligatory membership of stock market participants in self-regulating organisations. The document provides a realistic opportunity for self-regulating in the stock market to expand.

The Presidential Decree "On measures to ensure rights protection of investment funds' and investment companies' members", dated August 7, 1999, is aimed at regulating only a part of the problems which occur while closing investment funds and companies created for "paper" privatisation. It does not fundamentally resolve the issue of joint-investing institutions' activities in Ukraine.

The Law "On changes to the Law of Ukraine 'On securities and the stock-exchange'", dated June 3, 1999, is also worthy of mention. Finally, this document has included state external bonds and investment certificates in the list of securities.

Problems remaining unsolved

The following spheres of privatisation and stock market functioning require further legislative changes:

- Over 1,600 enterprises are not eligible for privatisation (the list of those enterprises is approved by the Law "On the list of legal entities under state ownership which are not subject to privatisation" dated July 7, 1999).

- There is a considerable need for a single law on joint-stock companies that would summarise the legislative base regarding joint-stock company activities in Ukraine in a form which is comprehensible both to investors, issuers, and mediators (its draft is submitted to the Verkhovna Rada). Also, there is a need for a new law on securities that would reflect all evolutional changes which took place in the market since the previous law adoption in 1992 (the new law is now being drafted by the government).
- Attracting public funds to the stock market is practically impossible without a law on joint-investing, which has been considered by the parliament for the second year now.
- The problem of compensation certificates utilisation is not resolved. After the Verkhovna Rada adopted the Resolution "On... the investigation of the circumstances of founding and activities of the Derzhinvest joint-stock company and the Finprom affiliated company" (September 15, 1998), which stopped privatisation using compensation certificates, the procedure of their circulation and utilisation still remains undefined.

Sectoral regulation

To evaluate changes in sectoral regulation we selected three industries that were most affected by legislative changes within the last year: agriculture, the power sector, and the banking sector are controlled by the state most of all, which is the core of the problems of regulating their activity. The problem of government interference in agricultural activity cannot be overcome without changing legislation to allow implementation of land reform. The lack of legislative mechanisms that enforce contract fulfillment is the cause of power sector's financial crisis, which, in turn, is responded to by the government's administrative sanctions. Weak economic policy destabilises the financial system, forcing the National Bank to resort to administrative actions that diminish the attractiveness of the banking system as a business field

Agriculture

Extreme state interference slows agricultural development in Ukraine. Without fundamental land reform, the abolishment of state interference in agricultural production and sales will be impossible.

Extreme state interference slows agricultural development in Ukraine. On one side, it is a natural results of market underdevelopment, and on the other side it prevents its creation. Without fundamental land reform, the abolishment of state interference in agricultural production and sales will be impossible. Existing limitations of land purchase, sale, lease, and pledge do not allow using land as collateral and prevent land transferring to effective owners.

During this year, two positive steps have been made on the way to land reform. The first one was directed at land lease adjustment and will promote more effective land usage; another step was directed at the development of mortgage procedures, encouraging commercial banks to lend to agricultural enterprises. But along with these achievements the proposed moratorium on application of bankruptcy procedures to agricultural enterprises, which will prevent land reform, was legislatively supported. Exempting agricultural enterprises from bankruptcy will restrain land transfers to effective owners.

Land lease

The Law "On land lease" dated October 6, 1998 was last year's most important legislative act regarding land reform. The law creates conditions for effective land usage through leasing.

The Law "On land lease" dated October 6, 1998 was last year's most important legislative act regarding land reform. The law creates conditions for effective land usage through leasing.

The law defines leasing relationships in detail and guarantees legal protection of lessees and lessors. But at the same time some of its provisions are defective:

- The law restricts lessee and lessor rights regarding the time horizon of rent payment. Article 19 of the law restricts the term of advance rent payment to one year. This regulation contradicts part 2 of the same article stating that size, form, and date of rent payment are determined in the lease contract with the parties' consent. Moreover, this restriction creates incorrect behavioral motives. The possibility to pay rent ahead for a long term would encourage lessees to follow contractual procedures, because if the contract was broken, rent would not be repaid.

- A separate duty rate for the land lease contract is not adopted. That is why a standard duty rate amounting to 5% of the contract value is used for such agreements. To pay this amount of money at the moment of contract signing is a heavy burden for lessees, as they have not yet collected any proceeds from land use.

It is necessary to amend some regulations of the Land Code of Ukraine to increase lease relationship effectiveness. In particular, the current Code edition states that the only entities having the right of collective land ownership are agricultural enterprises. Thus, if landowners do not want to be enterprise members, they are deprived of the right to lease out land collectively. It is possible to solve this problem through legislative adoption of collective and partial land ownership.

Mortgage

The draft law "On mortgage", submitted by the President but not approved by the Verkhovna Rada, determines land mortgage procedures, affording an opportunity to agricultural enterprises to receive non-public loans

The draft law "On mortgage", submitted by the President but not approved by the Verkhovna Rada, determines land mortgage procedures, affording an opportunity to agricultural enterprises to receive non-public loans. According to current legislation, mortgage relations are regulated by the Law of Ukraine "On collateral" because mortgages are a type of collateral where land or real estate are used. The necessity to adopt a special law "On mortgage" is conditioned by the fact that, according to current legislation, only land plots and perennial plantations belonging to citizens under private ownership may be used for mortgage. Such a formulation excludes the land of collective agricultural enterprises, which also need loans.

This matter is regulated by Article 4 of the draft law "On mortgage", stating that "land plots or shares of the right to collective land ownership" may be used for mortgage.

Adoption of the draft law "On mortgage" is an essential but insufficient condition for solving the problem of agricultural enterprise borrowing. The following steps should be taken to completely overcome this problem:

- update normative acts regulating land relations (the Land Code first of all);
- adopt new documents regulating land value assessment, registration of the right to land ownership and activity of financial organizations that will perform mortgage loan transactions.

Bankruptcy procedure

The provision of the Law "On amending the Law of Ukraine 'On bankruptcy'" on the application of bankruptcy procedures to agricultural enterprises will lead to preservation of loss-making enterprises

Increased effectiveness of land usage is impossible without imposing bankruptcy procedures as a method of transferring land to more effective owners. This process is restricted by the provision of the Law "On amending the Law of Ukraine 'On bankruptcy'" dated June 30, 1999 that prohibits suing agricultural enterprises. The moratorium on application of bankruptcy procedures to agricultural enterprises will lead to preservation of loss-making enterprises and further debt accumulation. The soonest possible application of the Law "On bankruptcy" in a new revision to agricultural enterprises will accelerate land transfer to more effective owners and promote land market development in Ukraine.

Power sector

In the power sector, the lack of effective mechanisms for contract enforcement has led to a dangerous increase in non-payments for supplied electricity. In response, the government approved resolutions to improve payment discipline in the sector.

In the power sector, the lack of effective mechanisms for contract enforcement has led to a dangerous increase in non-payments for supplied electricity. In response, the government imposed measures to improve payment discipline in the sector.

The main document was the Resolution of the Cabinet of Ministers dated March 24, 1999 "On urgent measures to stabilize financial conditions at enterprises in the power sector", which approved a new procedure for electricity supply to customers. According to the procedure, electricity supply should be stopped to those customers that do not pay in full for consumed electricity or do not follow the pre-determined schedule of arrears redemption. The procedure

also defines the mechanism for calculating the maximum amount of electricity supply to distribution companies, according to their level of payments for electricity. Thus, distributors have additional incentives to cut off debtors and pay up to electricity generating companies, while customers are motivated to settle accounts with suppliers on time.

Another Resolution of the Cabinet of Ministers "On approving measures aimed at improving financial conditions in the power sector of Ukraine in 1999–2000" dated May 19, 1999 envisages cessation of power supply to all debtors, except in cases stipulated by legislation. Implementation of the resolution increased the number of disconnected debtors, which led to improvement in payments for supplied electricity.

The resolution also envisages a set of measures for improving of power companies' financial conditions. It is planned to:

- draft a law on abolishing privileges in payments for electricity;
- make purchases of fuels from suppliers on a competitive basis;
- privatise or transfer to communal property those housing and social facilities that were not included in the capital funds of joint-stock companies but are still on their books.

Implementation of these measures will certainly stimulate the improvement of financial conditions in the power sector. But its ultimate normalisation will be impossible without solving the fundamental problems, particularly creating an effective mechanism for contract enforcement in the electricity market.

Banking sector

The main problem of banking sector regulation lies in the unstable regulation of bank activities. The instability is caused by attempts of the NBU to use regulatory tools to overcome financial crises.

Banking sector regulation is aimed at creating an effective banking system able to channel enterprise and household savings to competitive enterprises. The main problem lies in the unstable regulation of commercial bank activities. The instability is caused by attempts of the NBU to use regulatory tools to overcome financial crises. The threat of frequent changes in regulations (especially use of administrative instruments) discourages potential investments in the banking sector.

During the last year, some norms of banking legislation have been changed twice without any net effect. These included:

- prohibition and resumption of the inter-bank market;
- prohibition and permission to provide loans in foreign currency not under foreign-trade contracts;
- introduction and cancellation of interest rate restrictions on foreign loans provided to residents;
- prohibition and cancellation of import prepayment;
- establishing and dissolution of the Personal Deposit Fund.

One of the factors that limits bank incomes is the norm on an open foreign exchange position. The Resolution of the NBU board "On some issues related to the regulation of commercial banking" dated December 17, 1998 established the maximum value for the open foreign exchange position at the level of 35% of the bank's capital. Limited possibilities for arbitration operations in the currency market reduce the profitability of the banking sector.

The Resolution of the NBU board "On approving the Regulations obligatory cash reserving in the banking system of Ukraine" dated July 9, 1999 will have a lesser impact on the financial conditions of the banking system. According to the resolution, non-compliance with reserving requirements is considered as obtaining unauthorized credits from the NBU. Payment for using the credit is equal to the discount rate upon previous agreements with the NBU, and to the lombard rate without agreement. A positive effect of the resolution has been an increase in banking system discipline. The NBU's requirements will hasten the bankruptcy of constant violators, since their losses will increase. A negative aspect is the NBU's right to coordinate under-reserving, which creates room for unfairness. We consider it worthwhile to add a norm with a list of conditions under which payment for using unauthorized credits is equal to the discount rate.

The Resolution of the NBU board "On approving the Regulations on accounting and reporting at banking institutions of Ukraine" dated December 30, 1998 will have a positive effect on bank operations. It envisages the conversion of Ukrainian banks to international accounting standards. In 1999 the NBU introduced a new account plan

and obliged banks to conduct auditing according to international norms of reporting. This will foster the cooperation of Ukrainian banks with foreign clients and banks, since the new reporting form provides a more transparent and clear reflection of the bank's financial condition. For instance, evaluation of fixed capital, credit, and investment portfolios is made not on the basis of initial price, as it was made previously, but based on the market price.

The main legislative act that regulates commercial bank activities is the Law "On banks and banking" dated March 20, 1991, which has been changed and supplemented by 28 laws of Ukraine and the Cabinet of Ministers resolutions. In addition, many issues not regulated by the law are regulated by the NBU's bylaws, which are subject to frequent changes. The new draft law to be considered by the Verkhovna Rada in the current session:

- combines the significant part of the norms currently in force, while replacing many bylaws;
- defines a procedure for bank liquidation (bankruptcy), which has still not been regulated;
- simplifies the procedure for licensing and defines a single banking license;
- regulates relations between the bank and its founders.

The draft law "On the procedure for taxpayer arrears redemption to budgets and state target funds", which was submitted by the President of Ukraine in June and rejected by the Verkhovna Rada in September 1999, raised the controversial question of cancelling the *kartoteka* #2, which is seizure of funds without acceptance from the accounts of enterprises that have tax arrears without court sanction. The deputies approved a draft law which does not conceptually contradict the Presidential draft in the first reading. Abolishing the *kartoteka* will stimulate an increase in cash demand and rejection of the quasi-monetary instruments which enterprises had to use for ongoing current activity. Increasd banking resources and wider use of the banking system will foster increased lending and income of banks.

List of evaluated legislation

Regulation of economic activity			
Law of Ukraine	"On the protection of national producers from dumping imports"	dated December 22, 1998	№ 330-XIV
Law of Ukraine	"On the protection of national producers from subsidised imports"	dated December 22, 1998	№ 331-XIV
Law of Ukraine	"On topographic, geodesic, and cartographic activities"	dated December 23, 1998	№ 353-XIV
Law of Ukraine	"On amending Article 4 of the Law of Ukraine 'On entrepreneurial activities'"	dated January 12, 1999	№ 381-XIV
Law of Ukraine	"On hydrometeorological activities"	dated February 18, 1999	№ 443-XIV
Law of Ukraine	"On making changes to some laws of Ukraine concerning the activities of economic entities"	dated May 5, 1999	№ 622-XIV
Law of Ukraine	"On the state regulation of sugar production and sales"	dated June 17, 1999	№ 758-XIV
Law of Ukraine	"On the sources of government financing"	dated June 30, 1999	№ 783-XIV
Law of Ukraine	"On accounting and financial reporting in Ukraine"	dated July 16, 1999	№ 996-XIV
Presidential Decree	"On certain measures to deregulate entrepreneurial activity"	dated July 23, 1998	№ 817/98
Presidential Decree	"On the implementation of licensing activities of economic entities in the sphere of natural monopolies"	dated November 17, 1998	№ 1257/98
Presidential Decree	"On improving state control over quality and safety of food products, pharmaceuticals, and medical products"	February 1, 1999	№ 109/99
Presidential Decree	"On measures to improve rule-making"	dated February 9, 1999	№ 145/99
Presidential Decree	"On introducing a permit system in the sphere of entrepreneurial activities"	dated May 20,1999	№ 539/99

Presidential Decree	"On the state regulation of exports, imports, and wholesale and retail trade of petrochemicals"	dated June 11, 1999	№ 639/99
Presidential Decree	"On the Regulations on the Committee of Ukraine on Monopoly Production and Sale of Alcoholic and Tobacco Goods"	dated August 2, 1999	№ 941/99
Cabinet of Ministers Resolution	"On the procedure for state registration of business entities"	dated May 25, 1998	№ 740
Taxation policy			
Law of Ukraine	"On the levy rate for mandatory state pension insurance"	dated September, 30, 1998	№ 135-XIV
Law of Ukraine	"On the procedure for setting tax and levy rates (compulsory payments), and other elements of tax bases, and also tax privileges"	dated October 14, 1998	№ 171-XIV
Law of Ukraine	"On amending the Law of Ukraine 'On the levy for mandatory state pension insurance'"	dated October 22, 1998	№ 208-XIV
Law of Ukraine	"On writing off and restructuring tax arrears of coal-mining, coal- processing, and coal-mine building enterprises of the Ministry of the Coal Industry of Ukraine, and underground resource mining enterprises of the Ministry of Industrial Policy of Ukraine"	dated November 20, 1998	№ 268-XIV
Law of Ukraine	"On the fixed agricultural tax"	dated December 17, 1998	№ 320-XIV
Law of Ukraine	"On writing off and restructuring the tax arrears of taxpaying sugar refineries (works) on January 1, 1998, and agricultural enterprises on January 1, 1999"	dated February 5, 1999	№ 428-XIV
Law of Ukraine	"On amending the Law of Ukraine 'On the taxation of enterprise profit'"	dated April 6, 1999	№ 568-XIV
Law of Ukraine	"On the levy for development of viticulture, horticulture, and hop-growing"	dated April 9, 1999	№ 587-XIV

Law of Ukraine	"On amending the Law of Ukraine 'On excise rates and import duties for some goods (products)'"	dated May 5, 1999	№ 620-XIV
Law of Ukraine	"On amending Article 11 of the Law of Ukraine 'On the VAT'"	dated May 6, 1999	№ 624-XIV
Law of Ukraine	"On the stamp duty"	dated May, 13, 1999	№ 643-XIV
Law of Ukraine	"On amending the Law of Ukraine 'On the VAT'"	dated July 7, 1999	№ 854-XIV
Law of Ukraine	"On conducting an economic experiment at enterprises of Ukraine's mining and metallurgy sector"	dated July 14, 1999	№ 934-XIV
Law of Ukraine	"On amending Article 5 of the Law of Ukraine 'On the VAT'"	dated July 14, 1999	№ 942-XIV
Law of Ukraine	"On writing off and restructuring the tax arrears of water transport enterprises that appeared because Danube navigation limitation"	dated July 15, 1999	№ 965-XIV
Law of Ukraine	"On amending the Law of Ukraine 'On the levy for mandatory state pension insurance'"	dated July 15, 1999	№ 967-XIV
Presidential Decree	"On excise rates for oil products"	dated June 24, 1998	№ 680/98
Presidential Decree	"On the simplified taxation, accounting, and reporting system for small business entities"	dated July 3, 1998	№ 727/98
Presidential Decree	"On some changes in taxation"	dated August 7, 1998	№ 857/98
Presidential Decree	"On the stamp duty"	dated November 6, 1998	№ 1222/98
Presidential Decree	"On supporting agricultural producers"	dated December 2, 1998	№ 1328/98
Presidential Decree	"On amending the Presidential Decree 'On the simplified taxation, accounting, and reporting system for small business entities' № 727 dated July 3, 1998"	dated June 28, 1999	№ 746/99

Presidential Decree	"On cancelling the Cabinet of Ministers Resolution 'On introducing the system of gathering, sorting, transportation, processing, and utilisation of used packages (packaging)' № 1225 dated July 9, 1999"	dated July 22, 1999	№ 915/99
Resolution of the Verkhovna Rada	"On application of normative and legislative acts on taxation"	dated December 24, 1998	№ 363-XIV
Cabinet of Ministers Resolution	"On the specification of critical import goods "	dated June 18, 1999	№ 1080
Cabinet of Ministers Resolution	"On introducing the system of gathering, sorting, transportation, processing, and utilisation of used packages (packaging)"	dated July 9, 1999	№ 1225
Foreign trade			
Law of Ukraine	"On the implementation of special measures regarding imports to Ukraine"	dated December 22, 1998	№ 332-XIV
Law of Ukraine	"On scrap metal"	dated May 5, 1999	№ 619-XIV
Cabinet of Ministers Resolution	"On amending certain resolutions of the Cabinet of Ministers of Ukraine on setting the minimum customs values for light industry and agricultural products"	dated July 29, 1999	№ 1387
Foreign investment			
Law of Ukraine	"On concessions"	dated July 16, 1999	№ 997-XIV
Resolution of the Verkhovna Rada	"On amending the Resolution of the Verkhovna Rada of Ukraine 'On the procedure for implementing the Law of Ukraine 'On the regime of foreign investment'"	dated July 6, 1999	№ 823-XIV
Special economic zones			
Law of Ukraine	"On the special economic zone and the special regime for investment activity in Donetsk oblast"	dated December 24, 1998	№ 356-XIV
Law of Ukraine	"On the special regime for investment activity in Transcarpathia oblast"	dated December 24, 1998	№ 357-XIV

Law of Ukraine	“On the ’Yariv’special economic zone”	dated January 15, 1999	№ 402-XIV
Law of Ukraine	“On the ‘Kurortopolis Truskavets’ special economic zone as a tourist and recreation area"	dated March 18, 1999	№ 514-XIV
Law of Ukraine	“On the ‘Slavutych’special economic zone”	dated June 3, 1999	№ 721-XIV
Presidential Decree	“On the‘Zakarpattia’ special economic zone”	dated December 9, 1998	№ 1339/98
Presidential Decree	“On the special regime for investment activity in priority development areas of Luhansk oblast”	dated December 18, 1998	№ 1359/98
Presidential Decree	"On measures regarding creation of the ‘Reni’ special economic zone”	dated December 29, 1998	№ 1387/98
Presidential Decree	“On the Regulations for the Agency on Special (Free) Economic Zones”	dated May 17, 1999	№ 510/99
Presidential Decree	“On the’Interport Kovel’ special economic zone the”	dated June 22, 1999	№ 702/99
Presidential Decree	“On the special regime for investment activity in the city of Shostka, Sumy oblast”	dated June 27, 1999	№ 726/99
Presidential Decree	“On the special regime for investment activity in priority development areas of Chernihiv oblast”	dated June 27, 1999	№ 729/99
Presidential Decree	“On the special regime for investment activity in priority development areas of Volyn oblast”	dated June 27, 1999	№ 730/99
Presidential Decree	“On the special regime for investment activity in the city of Kharkiv”	dated June 27, 1999	№ 731/99
Presidential Decree	“On the special regime for investment activity in priority development areas of Zhytomyr oblast”	dated June 27, 1999	№ 732/99
Presidential Decree	“On the special regime for investment activity in priority development areas and the ‘Crimea Port’ special economic zone”	dated June 27, 1999	№ 740/99
Presidential Decree	“On the ‘Mykolaiv’ special economic zone”	dated June 28, 1999	№ 758/99

Presidential Decree	"On the 'Porto-Franko' free economic zone in areas of the Odesa Marina and Commercial Port"	dated June 28, 1999	№ 760/99
Contract enforcement			
Law of Ukraine	"On executor enforcement"	dated April 21, 1999	№ 606-XIV
Law of Ukraine	"On amending the Law of Ukraine 'On bankruptcy'"	dated June 30, 1999	№ 784-XIV
Law of Ukraine	"On Ukraine joining the Geneva Conventions of 1930 imposing a Single Law on Bills of Exchange and promissory notes"	dated July 6, 1999	№ 826-XIV
Law of Ukraine	"On Ukraine joining the Geneva Conventions of 1930 on certain coalitions of laws on Bills of Exchange and promissory notes"	dated July 6, 1999	№ 827-XIV
Law of Ukraine	"On Ukraine joining the Geneva Conventions of 1930 on stamp duty regulating Bills of Exchange and promissory notes"	dated June 6, 1999	№ 828-XIV
Presidential Decree	"On the procedure for collecting taxpayer debts to budgets and state target funds"	dated June 28, 1999	№ 754/99
Privatisation and the stock market			
Law of Ukraine	"On changes to the Law of Ukraine 'On securities and the stock exchange'"	dated June 3, 1999	№ 719-XIV
Law of Ukraine	"On the list of legal entities under state ownership which are not subject to privatisation"	dated July 7, 1999	№ 847-XIV
Law of Ukraine	"On changes to some laws of Ukraine aimed at stimulating investment activities"	dated June 15, 1999	№ 977-XIV
Presidential Decree	"On non-agricultural land sales"	dated January 19, 1999	№ 32/99
Presidential Decree	"On the State Privatisation Program"	dated February 24, 1999	№ 209/99
Presidential Decree	"On amending Presidential Decree № 210 dated June 15, 1993"	dated May 28, 1999	№ 587/99
Presidential Decree	"On the peculiarities of privatisation of unfinished construction projects"	dated May 28, 1999	№ 591/99

Presidential Decree	"On the general functioning principles of the National Depository of Ukraine"	dated June, 22 1999	№ 703/99
Presidential Decree	"On the membership of securities market professionals in self-regulating organisations"	dated June 27, 1999	№ 728/99
Presidential Decree	"On the National Agency of Ukraine for State Corporate Rights Management"	dated July 7, 1998	№ 752/98
Presidential Decree	"On some issues of privatisation in the power sector"	dated August 2, 1999	№ 944/99
Presidential Decree	"On measures to ensure rights protection of investment funds' and investment companies' members"	dated August 7, 1999	№ 968/99
Presidential Decree	"On the Regulations on the National Agency of Ukraine for State Corporate Rights Management"	dated September 2, 1998	№ 969/98
Resolution of the Verkhovna Rada	"On authorising the Special Monitoring Committee of the Verkhovna Rada on Privatisation as an interim committee of the investigation of the circumstances of founding and activities of the Derzhinvest joint-stock company and the Finprom affiliated company, and announcing Presidential Decree № 233 dated March 27, 1998"	dated September 15, 1998	№ 108-XIV
Sectoral regulation			
Law of Ukraine	"On land lease"	dated October 6, 1998	№ 161-XIV
Cabinet of Ministers Resolution	"On urgent measures to stabilize financial conditions at enterprises in the power sector"	dated March 24, 1999	№ 441
Cabinet of Ministers Resolution	"On approving measures aimed at improving financial conditions in the power sector of Ukraine in 1999–2000"	dated May 19, 1999	№ 845
Resolution of the NBU board	"On some issues related to the regulation of commercial banking"	dated December 17, 1998	№ 524
Resolution of the NBU board	"On approving the Regulations on accounting and reporting at banking institutions of Ukraine"	dated December 30, 1998	№ 566
Resolution of the NBU board	"On approving the Regulations on obligatory cash reserving in the banking system of Ukraine"	dated July 9, 1999	№ 332

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